



STATE OF CONNECTICUT

INSURANCE DEPARTMENT

Testimony Insurance and Real Estate Committee March 15, 2016

Senate Bill No. 436 – An Act Concerning Insurer Corporate Governance Annual Disclosure and the Regulation of Risk Retention Groups.

Senator Crisco, Representative Megna, Rankings Members, and members of the Insurance and Real Estate Committee, the Insurance Department would like to thank the Committee for introducing this initiative on our behalf and raising **Senate Bill No. 436 An Act Concerning Insurer Corporate Governance Annual Disclosure and the Regulation of Risk Retention Groups**.

Senate Bill No. 436 would enhance the Department's core mission of consumer protection by:

- Giving the Department greater authority over a domestic insurer or insurance group by requiring a confidential annual disclosure of corporate governance practices.
- Enhancing the Department's regulatory oversight of Risk Retention Groups (RRGs), self-insurers created by the federal government and whose regulatory framework has historically pre-empted state laws.

Corporate Governance

Since the 2008 financial crisis, it became important that state insurance regulators have a better understanding of insurers' governance practice. As a result, the National Association of Insurance Commissioners (NAIC), set standards in the form of a 2014 model law that requires a domestic insurer to provide confidential corporate governance disclosure annually to its home-state regulator as part of the solvency-monitoring process. By adopting this standard, Connecticut will respond to existing regulatory needs and it will assist Connecticut and other U.S. insurance regulators in achieving greater consistency with international standards.

Additionally, the Department anticipates that adopting this legislation, which would take effect, January 1, 2017, will allow the Department meet future NAIC accreditation requirements.

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Risk Retention Groups

Risk Retention Groups are a creation of federal law and essentially are entities allowed to self-insure their commercial liability risk to create their own insurance company. However, they have operated largely outside the framework of state law and have been primarily regulated by the state in which they are domiciled even when selling insurance coverage in other states.

Consumers are ill-served by what we believe is a dangerous gap in regulation and we need only point to a recent example of an RRG that went bankrupt leaving dozens of Connecticut policyholders – mostly small business owners – exposed without liability coverage.

The Indemnity Insurance Company (IIC), domiciled in Delaware, was one of the largest RRGs providing liquor liability coverage for bars and restaurants around the country, including many establishments here in Connecticut.

Two years ago the company was declared insolvent by Delaware regulators, ordered into liquidation and had to cancel all its policies. Policyholders lost their premiums and coverage. There was no insurance company to pay damages or legal fees for pending lawsuits. Liability lawsuit judgments against the policyholders could not be paid. Plaintiffs only course was to go directly against the policyholders' assets. At the time of the liquidation, there were 68 liquor liability lawsuits pending against IIC policyholders in Connecticut.

Additionally, the Connecticut Insurance Guaranty Fund, which covers policyholders when companies go bankrupt, could not step in due to federal preemption of risk retention groups.

Senate Bill 436 will establish sound corporate governance standards for RRGs and amend provisions within Chapter 698e concerning risk retention groups to closely track with provisions of NAIC Model Risk Retention Act, which was recently revised in 2011.

Finally, adopting these provisions is of critical importance in maintaining the Department's NAIC accreditation. The NAIC Financial Regulation Standards and Accreditation Program revised its standards to require states to have laws enacted **no later than January 1, 2017**, that are substantially similar to the NAIC Model Risk Retention Act provisions governing corporate governance principles.

The Insurance Department thanks the Insurance and Real Estate Committee for the opportunity to provide this testimony in support of S.B. 436. The Department respectfully requests the Committee give a favorable substitute report to S.B. 436. These new provisions would be effective January 1, 2017 and are summarized in the attachment at the end of this testimony, along with proposed changes to the text of the bill.

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Senate Bill No. 436 (Raised)
(LCO No. 2931)

Summary

Corporate Governance
(Section 1)

[Comment: The Insurance Department requested legislation to adopt the NAIC Corporate Governance Annual Disclosure Model Act (Model Act). The Department notes that the Legislative Commissioner's Office (LCO) did not incorporate into Raised Bill 436 Section 1.A. of the Model Act concerning the purpose of the legislation.]

Subsection (a) contains definitions.

Subsection (b) contains the annual corporate governance annual disclosure (CGAD) and filing requirements. ***[Comment: The Insurance Department requests the insertion of the following sentence that was omitted in the bill in order to conform with the Model Act Section 3.C.: at the end of line 40, insert: "An insurer not required to submit a CGAD under this subsection shall do so upon the Commissioner's request."]***

Subsection (c) specifies the contents of the CGAD.

Subsection (d) (1) specifies that for purposes of completing the CGAD, the insurer or insurance group may provide the required information on governance activities that occur on any level of their corporate structure, depending on the structure of the insurer or group's corporate governance system as noted therein; (2) the insurer or group may utilize other existing documents that furnish information comparable to that required in subsection (c); (3) allows the insurer or group to have some discretion over responses to the CGAD so long as the responses convey sufficient information to the Commissioner regarding corporate governance, structure and policies, and requires the insurer or group to maintain any CGAD-related documents and supporting information and make such available to the Commissioner upon request; and (4) requires the CGAD to include the signature of the insurer or group's CEO or corporate secretary attesting to the fact that the insurer or group has implemented the policies set forth in the CGAD. ***[Comment: The Insurance Department requests that in line 143, after the word "group" the following word be inserted: "should".]***

Subsection (e) provides for the confidentiality and privileged status of corporate governance documents, materials or other information, including the CGAD that are obtained by, created by or disclosed to the Commissioner or any other person pursuant to this section. ***[Comment: 1. The Department requests in line 188, after the word "section" the insertion of the following: "are recognized by this state as being proprietary and to contain trade secrets and".***

[Comment: 2.

The Insurance Department requests the insertion of the following sentence that was omitted in the bill in order to conform with the Model Act: at the end of line 197, insert: "Nothing in this

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*subsection shall be construed to require written consent of the insurer before the Commissioner may share or receive confidential documents, materials or other CGAD-related information pursuant to subdivision (3) of this subsection to assist in the performance of the Commissioner's regular duties." **Comment 3.** The Insurance Department requests that in line 266, the word "subsection" be replaced with "section" so that there will be no waiver of any applicable privilege or claim of confidentiality in any of the CGAD-related information as a result of disclosure to the Commissioner under this section.]*

Subsection (f) authorizes the Commissioner to retain, at the insurer's expense, third-party consultants, including attorneys, actuaries, accountants and other experts not otherwise a part of the Commissioner's staff as may be reasonably necessary to assist in reviewing the corporate governance annual disclosure and related information or the insurer's compliance with this Act.

Subsection (g) imposes a \$175 per day penalty for failure to file the corporate governance annual disclosure statement with the Commissioner.

Correlation Table

NAIC Model Act

Raised Bill No. 436

Section 1. Purpose and Scope.

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|----|--------------------------|
| A. | Omitted |
| B. | Lines 289-292 |
| C. | Omitted, but see line 31 |

Section 2. Definitions.

Lines 1-29

Section 3. Disclosure Requirement.

- | | |
|----|---------------|
| A. | Lines 30-40 |
| B. | Lines 178-184 |
| C. | Omitted |
| D. | Lines 138-153 |
| E. | Lines 270-274 |

F. (NAIC Model Reg. Sec. 4.F. used) Lines 154-161

(NAIC Model Reg. Sec. 4.G. used) Lines 41-44

Section 4. Rules and Regulations.

Omitted

Section 5. Contents of CGAD.

- | | |
|--------------------------------|------------------------|
| A. | Lines 162-167, 170-174 |
| B. | Lines 174-177 |
| (NAIC Model Reg. Sec. 5. used) | Lines 45-137, 167-170 |

Section 6. Confidentiality.

- | | |
|----|---------------|
| A. | Lines 185-197 |
| B. | Lines 198-203 |
| C. | Lines 204-227 |
| D. | Lines 267-269 |
| E. | Lines 263-266 |

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Section 7. NAIC and Third-party Consultants.	
A.	Lines 275-282
B.	Lines 282-283
C.	Omitted, but see lines 211-217
D.	Lines 284-288
E.	Lines 228-262
Section 8. Sanctions.	Lines 293-299
Section 9. Severability Clause	Omitted, but see C.G.S. § 1-3

Risk Retention Groups (§§ 2 – 8)

Sec. 2 amends the definitions in Section 38a-250 to add “NAIC”, and to revise definition “plan of operation or a feasibility study” to specify that the analysis contained in any such plan or study shall include activities for each state in which the risk retention group (RRG) intends to operate.

Sec. 3 amends Conn. Gen. Stat. § 38a-251 concerning the licensure and regulation of RRGs chartered in this state. New provisions in **subsection (b)** will require RRGs to submit for the Commissioner’s approval an appropriate revision within ten days of any subsequent material change in any item of the plan of operation or in the feasibility study, and the RRG may not offer any additional kinds of liability insurance in any state until such revision is approved.

[Comment: the Insurance Department requests this language to be modified as follows: 1. In line 465, after the word “group” insert “seeking to be chartered in this state”; 2. In lines 468-469 delete the words “not later than ten days after any such change occurs or has been made”; 3. In line 471, insert before the word “unit” the words: “or operate under any other material change including changes in rates”. New provisions in subsection (c) will require RRGs to provide the Commissioner at the time of filing its application for a charter, information on the identity of the initial members of the RRG, the RRG organizers, persons who will provide administrative services or otherwise influence or control coverages to be afforded, and the states in which the RRG intends to operate.

Sec. 4 Will establish corporate governance standards for RRGs. (A majority of independent directors on the RRG board of directors, audit committee, adoption and disclosure of governance standards, adoption of business conduct and ethics for officers, directors and employees, and reporting of material non-compliance of such standards to the Commissioner). ***[Comment: These provisions are based on the NAIC Model Risk Retention Act Sec. 3.D. which are required in order for the Insurance Department to maintain its accreditation by the NAIC. Comment: the Insurance Department requests that in lines 547-550 the following words be deleted: “notified the commissioner in writing of its intent to enter into such contract at least thirty days prior to entering into such contract and the commissioner has not disapproved such contract with such period” and in lieu thereof, insert the following words: “submitted such change in the plan of operation and received the Commissioner’s prior approval.”]***

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Sec. 5 amends Conn. Gen. Stat. § 38a-252. The risk retention group shall submit a copy of any material revision to its plan of operation or feasibility study required by subsection (b) of section 38a-251 within thirty days of the date of the approval of such revision by the Commissioner of its chartering state, or if no such approval is required, within thirty days of filing.

Sec. 6 makes minor changes to Conn. Gen. Stat. § 38a-253 concerning submission of information to the Commissioner from RRGs domiciled outside Connecticut.

Sec. 7 makes a minor change to Conn. Gen. Stat. § 38a-255 to require in addition to every policy, that every application form for insurance from a risk retention group shall contain a notice that the risk retention group may not be subject to all the insurance laws and that the insurance guaranty association funds are not available for the risk retention group.

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